

## **Title: Discovery Team – Tax Gap BCP No. 2a**

**Purpose:** Address the Use Tax Gap by creating a Discovery Team to investigate use tax leads.

**Summary:** This proposal establishes a Team which will develop and investigate new and previously untapped sources of information for the purpose of developing solid informational leads on California businesses and taxpayers which are not currently required to be registered with the Board of Equalization, but incur use tax liabilities as a result of untaxed purchases made from outside the state. This Team's effort will help to reduce the current Use Tax Gap, educate taxpayers and level the playing field for California retailers who currently collected the tax but may be losing sales as a result of taxpayers choosing to make purchases outside the state.

Note: The Legislative Analysts Office recommended at this year's Senate budget hearings that the Board of Equalization consider establishing a discovery unit which would aid in addressing the Tax Gap.

### **Alternatives:**

1. Discovery Team
  - a. Total Resource Needed (two-year limited-term):
    - 26 positions and \$2,026,000 in FY 2006-07
    - 26.5 positions and \$1,992,000 in FY 2007-08
  - b. Benefit-to-Cost Ratio: 4.0 to 1.
2. Use Existing Resources
  - a. Revenue generated by the Discovery program will be offset with loss of revenue from existing programs due to redirection of revenue-generating positions.
3. Phase-in Discovery Team
  - a. Total Resource Needed (two-year limited-term):
    - \$1,993,000 in FY 2006-07
    - \$1,992,000 in FY 2007-08
  - b. Benefit-to-Cost Ratio: 4.0 to 1.

### **Staff Recommendation:**

Approve Alternative I: Establish 26.0 positions for two-year limited term to address the Use Tax Gap that provides at a minimum a benefit-to-cost ratio of 4.0 to 1.

**Title: Public Awareness Campaign for Use Tax – Tax Gap BCP No. 2b**

**Purpose:** Address the Use Tax Gap through a media campaign.

**Summary:** This proposal offers a number of alternatives for a media campaign to address the payment of use tax liabilities by unregistered businesses and taxpayers contributing to the \$1.8 billion tax gap. The options vary significantly from a broad media campaign, similar to our recent Tax Amnesty effort, to a more modest and highly focused effort aimed at tax preparers. Each alternative is intended to compliment other tax gap closing efforts. The goal of the media campaign is to raise future compliance of unregistered businesses and taxpayers through outreach and education efforts by making the public aware of tax laws, reporting requirements, and increased enforcement.

**Alternatives:**

1. Board Media Campaign
  - a. Total Resource Needed: \$2.5 million for private contract services and other media related resources.
  - b. Benefit-to-Cost Ratio: Unmeasureable at this time. Would be reflected in subsequent years of use tax reportings.
2. Moderate Media Campaign
  - a. Total Resource Needed: \$750,000 focused on campaign targeting those most likely to have unreported and unpaid use tax liabilities.
3. Expand existing staff with three 2-year limited-term positions and \$200,000 for expenses
  - a. Would not include internal resources to produce advertisements or public service announcements.
  - b. Limit the compliance generated by a full-scale publicity effort.
  - c. May paralyze the long-term success of the BOE's program.
4. Focused Campaign on Tax Professionals
  - a. Total Resource Needed: \$250,000 one-time funding.
  - b. Benefit-to-Cost Ratio: Unmeasureable at this time but would expect to obtain a minimum of 4.0 to 1.

**Staff Recommendation:**

Approve Alternative 4: Recommend a highly focused campaign effort on Tax Professionals for a one-time funding of \$250,000 that provides at a minimum a benefit-to-cost ratio of 4.0 to 1.

## **Title: Agricultural Inspection Station Tax Leads – Tax Gap BCP No. 2c**

**Purpose:** Address the Sales and Use Tax Gap by detecting and identifying property being brought into California without payment of Sales and Use Taxes.

**Summary:** Under this proposal, the Board of Equalization (BOE) would enter into an interagency agreement with the California Department of Food and Agriculture (CDFA). The CDFA staff at an assigned agricultural inspection station would forward bills of lading, fuel tax licenses, and vehicle registration documents from motor carriers transporting products and tangible personal property that may be subject to use tax. BOE staff would analyze all the forwarded information for viable leads, investigate the leads, and then assess and collect taxes due.

### **Alternatives:**

1. Implement a two-year pilot identifying tax leads at one CDFA inspection station staffed by CDFA employees.
  - a. Total Resources Needed:
    - 25 positions for a two-year limited term.
    - FY 2006-07: \$2,964,000
    - FY 2007-08: \$2,640,000
  - b. Benefit-to-Cost Ratio: 6.0 to 1
2. Implement a two-year pilot identifying tax leads at two CDFA inspection stations with both stations staffed by CDFA employees.
  - a. Total Resources Needed:
    - 45 positions for a two-year limited term.
    - Estimated two-year cost is \$11,200,000.
3. Maintain current operations.
4. Implement a two-year pilot identifying tax leads at two CDFA inspection stations with one of the stations staffed by BOE employees.
  - a. Total Resources Needed:
    - 25 positions for a two-year limited-term.
    - FY 2006-07: \$2,813,000
    - FY 2007-08: \$2,505,000
  - b. Estimated Benefit-to-Cost Ratio: 4.8 to 1. This ratio is lower than Alternative 1 because there will be 3 less BOE staff working lead investigations. Instead, this staff will be placed at the second CDFA inspection station.

### **Staff Recommendation:**

Approve Alternative 1: Implement a two-year pilot identifying tax leads at one CDFA inspection station staffed by CDFA employees.

**Title: Enforcement of consumer Purchases of Tobacco Products from Out-of-State Sellers – Tax Gap BCP No. 2d**

**Purpose:** Address the Tax Gap on cigarette and tobacco sales.

**Summary:** This proposal offers two alternatives to address the Tax Gap of cigarette and tobacco sales through the Internet and mail orders. The options vary from establishing additional positions to increase enforcement against the growth of consumers that are purchasing untaxed tobacco products by Internet and mail order to using of existing resources. With adequate resources, BOE can, on a timely basis, register the consumers, mail tax returns to consumers, process incoming tax payments, and perform basic audit examinations of sales invoice and common carrier records to identify and assess unregistered consumers and businesses that have imported the largest number of untaxed shipments of cigarettes or tobacco products.

**Alternatives:**

1. Enforcement Resources
  - a. Total Resources Needed (two-year limited-term):
    - FY 2006-07: 22.5 positions and \$2,075,000
    - FY 2007-08: 14.3 positions and \$1,141,000
  - b. Benefit-to-Cost Ratio: 14.8 to 1.
2. Maintain Current Resources
  - a. Does not address the new workload and the estimated tax gap of approximately \$52 million in assessments that could contribute additional tax revenue to the state's General Fund and Special Funds.

**Staff Recommendation:**

Approve Alternative 1: Establish 22.5 positions for two-year limited-term to address the tax gap of cigarette and tobacco sales through the Internet and mail orders that provides a benefit-to-cost ratio of 14.8 to 1.

## **Title: Retail Licensing Enforcement – Tax Gap BCP No. 2e**

**Purpose:** Address the Use Tax Gap by identifying and registering entities that actively engage in business in California and sell tangible personal property without a seller's permit.

**Summary:** The positions and resources requested will be used to implement a two-year pilot Licensing Sweep Program. The requested positions will be utilized to conduct sales and use tax licensing compliance inspections in two of California's largest metropolitan areas, the Greater San Francisco Bay Area and the Los Angeles Metropolitan Area.

### **Alternatives:**

1. Implement a two-year Licensing Sweep Pilot Program with 33 positions.
  - a. Total Resources Needed:
    - 33 positions for a two-year limited term.
    - FY 2006-07: \$3,535,000
    - FY 2007-08: \$3,181,000
  - b. Benefit-to-Cost Ratio: 7.9 to 1
2. Implement a two-year Licensing Sweep Pilot Program with 16 positions.
  - a. Total Resources Needed:
    - 16 positions for a two-year limited term.
    - Estimated two-year cost is \$3,600,000.

### **Staff Recommendation:**

Approve Alternative 1: Implement a two-year Licensing Sweep Pilot Program with 33 positions.